Urban Financing in India

Why in news?

A recent report by World Bank say that India needs approximately 70 lakh crore rupees by 2036 to meet its urban infrastructure needs.

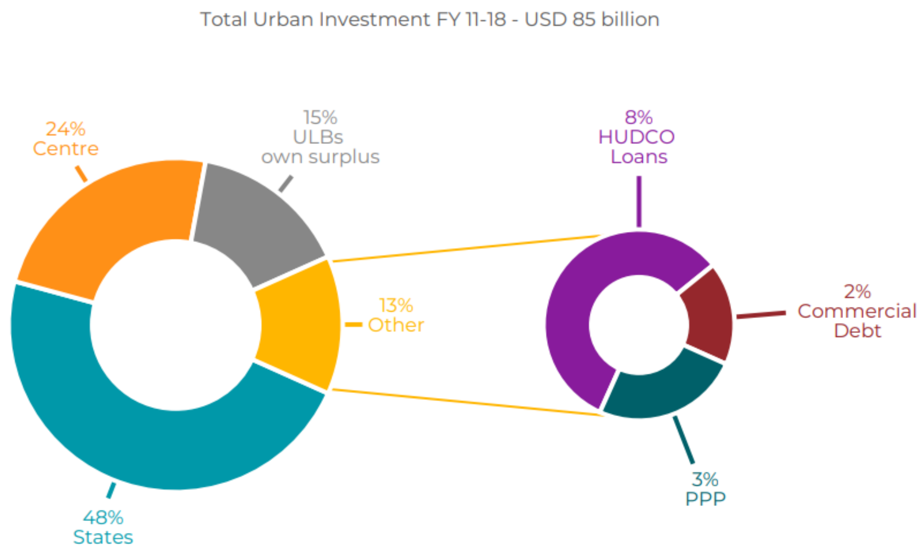
What is urban financing?

> *Urbanization is the process of people moving from rural to urban areas, and the corresponding growth in the number of people living in cities.*

- **Urban financing** – It is the process of securing the funds needed to improve and expand a city's physical infrastructure.
- **Source of urban revenues in India**

Revenue Head	Sources of Revenue
Tax Revenue	Property tax, advertisement tax, tax on animals, vacant land tax, entertainment tax, surcharge on stamp duty, profession tax, Motor vehicles tax.
Non-tax Revenue	User charges, municipal fee, sale & hire charges, lease amount.
Assigned/shared revenue	ULBs receive a percentage of taxes levied and collected by the state government.
Grants-in-aid	Grants from central government and state government under various projects and schemes.
Loans	Loans borrowed by the local authorities for capital works from HUDCO, LIC, State and Central Governments, Banks and Municipal Bonds.

- **Shortfall in financing** – Current annual investment of 1.3 lakh crore rupees falls short of the required 4.6 lakh crore rupees.
- To meet the demands of its fast-growing urban population, the government would *need to invest 84,000 crores rupees* over the next 15 years, an average of 5,500 crores rupees each year



Due to rapid urbanization, urban local bodies will be home to 40% of the population by 2036, and urban areas contribute almost 70 % to GDP.

What are the current issues in urban financing?

- **Stagnant municipal finances** – Municipal tax revenues have risen by 8% in past decade which shows only modest growth.
    - Municipal revenue stuck at 1% of GDP since 2002.
- **Inefficient tax collection** – Low service charges for municipal services undermine financial sustainability and viability.
    - Property tax contributes *only 0.15% of GDP*.
- **Low cost recovery** – The cost recovered on implemented projects in urban utilities is very low compared to other large middle-income countries.
- **Weak absorptive and implementation capacity** – It limits overall infrastructure delivery due to institutional weaknesses like weak strategic planning to develop pipeline of viable projects, low capacity to design and structure complex projects.
- **Low fund utilization** – As per 15th finance commission report, *23% of municipal revenue* remains unspent.
- **Underutilization of central schemes** – Urban local bodies were able to *spend only 2/3rd* of funds under schemes like Smart Cities Mission and AMRUT schemes.
- **Dependency on transfer payment** – ULBs are highly dependent on central and state grants which reduced their ability to funds.
- **Declining public-private partnerships** – Private debt financing has primarily been raised by a few large ULBs across the country, with cities from only 7 states accounting for all municipal bond issuances in India.
- Private investments dropped from 8,353 crore rupees in 2012 to 467 crore rupees in 2018.
- **Restrictive inter-governmental framework** – It reduces accountability and incentives for city agencies to invest more ambitiously in infrastructure.
- **Highly centralized** – States control over ULB financing which is opposite of international best practice, is not conducive to create environment for private

financing.

- **Weak fiduciary capacity** – The quality and data of city agencies undermines investor confidence and creditworthiness.

What are the reforms suggested by the World Bank?

- **To strengthen municipal governance** – By revising state municipal legislation to give them more authority.
- **Structural reforms** - The fiscal transfer system (at both national and state levels) should move to a *more stable, formula-based, and unconditional fiscal transfer regime.*
- **Improve creditworthiness** – By addressing revenue constraints through increasing property taxes, user fees and service charges from the current low bases substantially in real terms.
- **Diversify funding sources** – Use of municipal bonds, land-value capture, and attract private investment through better PPP models.
- **Decoupling project preparation** – Project preparation must prioritize financial, social, and environmental sustainability to ensure long-term success.
- **Improving cities absorptive capacity –** Supporting cities with *strategic multi-year capital investment*, financial planning and building a pipeline of investment projects.
- **Adopt digital public infrastructure (DPI) –** To streamline services like transport and utilities using digital technologies.
- **Increase decentralization –** Empowering local governments and communities is essential for sustainable urban development.
- **Capacity building** – Through facilitation, technical assistance, and removing market frictions
- **Establish a dedicated Support Unit** – Such as ***Cities Investment unit*** within an appropriate Ministry to focus on infrastructure finance to assist specific cities.
  - This Unit can *nurture partnerships between stakeholders*.
- **Integrated urban development –** Urban transport projects, such as metro rail systems, should be integrated with ***land-use planning*** to *optimize resource utilization* and reduce commuting distances.

What lies ahead?

- Allocate *minimum 10% of income tax collected* from cities for urban infrastructure development.
- Engage citizens in identifying needs and designing solutions.
- Coordinate between government, private sector, and citizens for innovative solutions.
- Ensure regular elections and accountability in urban local bodies.

Reference

[The Hindu |India’s urban infrastructure financing]